IN THE

Supreme Court of the United States

October Term, 1961

No. 54

UNITED STATES OF AMERICA and ERNEST J. TIBERINO, JR., Special Agent, Internal Revenue Service,
Petitioners,

v.

MAX POWELL and WILLIAM PENN LAUNDRY, INC.

On Petition for a Writ of Certiora... to the United States Court of Appeals for the Third Circuit.

MEMORANDUM ON BEHALF OF RESPONDENTS.

SCHNADER, HARRISON, SEGAL & LEWIS,
1719 Packard Building,
Philadelphia, Penna. 19102,
Of Counsel.

BERNARD G. SEGAL,
SAMUEL D. SLADE,
Attorneys for Respondents.

International, 711 So. 50th St., Phila., Pa. 19143

IN THE

Supreme Court of the United States.

OCTOBER TERM, 1963.

No. 944.

UNITED STATES OF AMERICA AND ERNEST J. TIBERINO, JR., SPECIAL AGENT, INTERNAL REVENUE SERVICE,

Petitioners

v.

MAX POWELL AND WILLIAM PENN LAUNDRY, INC.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

MEMORANDUM ON BEHALF OF RESPONDENTS.

In this case, the Internal Revenue Service has advanced for decision a claim of statutory power which the Service has frequently asserted but has rarely placed squarely in issue. Specifically, the Internal Revenue Service asserts that, by virtue of the broad language of Section 7602 of the Internal Revenue Code of 1954, 26 U. S. C. 7602, it possesses unlimited power to compel the production of a taxpayer's books and records and to require the giving of testimony in response to administrative summons. Where the administrative demand is resisted, it is the posi-

tion of the Service that it can obtain judicial enforcement of its demand on the basis of its bare statement to the enforcing court that the Service has determined the demand to be reasonable and necessary.

Here, an administrative demand was made for the production of all of respondent's books and records for its tax years 1958 and 1959 (R. 23a). Respondent's returns for those years had been timely filed and had been earlier examined by Internal Revenue Service Agents who had assessed deficiencies which were promptly paid (R. 22a-23a). The demand for production of respondent's books and records was first made on February 26, 1963, more than three years after the returns for 1958 and 1959 had been filed (R. 23a).

At an administrative hearing held on March 25, 1963, the Special Agent, who had caused the summons to be issued and who conducted the hearing, declined to offer any justification for the decision to re-examine the years in question (R. 23a-24a, 17a). This position, that no justification would or need be advanced for the decision by the Service to re-examine respondent's books and records for these closed years, was deliberately adhered to by the Service in the proceeding which it brought in the District Court for the Eastern District of Pennsylvania to compel compliance with the summons (R. 3a-5a). The pleading whereby the compliance proceeding was instituted rested on the issuance of the summons and the refusal of respondent to comply, and demanded an order directing such compliance. Attached to the pleading was an affidavit by the Special Agent which contained, *inter alia*, a conclusory statement as to his suspicion of fraud. In the district court proceeding, counsel for the Internal Revenue Service declined to offer testimony or proof in support of the administrative demand (R. 31a-32a).

The district court expressed dissatisfaction with the refusal of the Service to present testimony (R. 31a-32a, 36a), and stated agreement with respondent's position (R.

37a-38a). However, the district judge determined upon a compromise order whereby he permitted examination of respondent's books and records for one hour only (R. 45a).[1]

From the outset, respondent has challenged the Service's claim to an unlimited right of access to its books and records. Respondent bases its position on Sections 6501, 7605 and 7604 of the Internal Revenue Code. Section 6501 limits the power of the Service to assess and collect taxes to a period of three years after the filing of the return in question, unless fraud or a willful attempt to evade taxes can be shown. Section 7605 provides that no taxpayer shall be subjected to "* * * unnecessary examination or investigations * * *". Section 7604(b) provides for judicial enforcement of an Internal Revenue summons "* * * if satisfactory proof is made * * *" in support of the application for enforcement.

Based on these statutory provisions, respondent requested, at the administrative hearing, that some justification be advanced by the Service for the demanded reexamination and stated that if some justification were offered, respondent would reconsider its position (R. 16a-17a). Respondent's position, of course, was that Section 7602, upon which the Service relied, must be read in the light of these other pertinent sections of the Internal Revenue Code. As already noted, the Service advertently declined to offer any support for its demand either at the administrative level or in the district court proceeding.

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1. The petition for certiorari in this case refers to the curious order of the district court as containing "* * * certain limitations not here pertinent * * *" (Pet., p. 6). The district court order, limiting examination to one hour, was stayed in connection with the appeal and the parties stipulated that, if respondent were not successful on appeal, the Service would not be held to the one hour limitation. We have, however, described the district court's action specifically since elsewhere the petition for certiorari states that "* * * the district court was fully warranted in enforcing the summons" (Pet., p. 12). The transcript shows that the district judge really avoided resolution of the issue presented (R. 34a, 37a-39a).

On appeal, respondent's position was sustained by the Court of Appeals for the Third Circuit in an opinion by Judge Hastie which, we respectfully submit, construes the pertinent statutory provisions correctly. Judge Hastie took as his point of departure the question of a court's responsibility when called upon to enforce a demand by Internal Revenue such as that here involved. On the basis of Section 7604(b), which requires a "hearing" on the application to enforce the administrative summons and the production of "satisfactory proof" at that hearing, Judge Hastie rejected the argument of the Service that the basis for a Special Agent's suspicion of fraud was not a matter of judicial cognizance.[2] Absent the discovery by the Service of some facts which would cause a reasonable man to suspect fraud in a return for an otherwise closed year, and a disclosure of these facts, Judge Hastie held that a reexamination of a taxpayer's records, such as that demanded in this case, was "unnecessary" within the meaning of Section 7605(b) and that enforcement of the administrative summons must be denied.

In reaching its conclusion the court below correctly recognized that, on careful analysis, there is no real conflict among the decisions. An analysis of **United States v. Ryan**, 320 F. 2d 500 (C. A. 6, 1963), in which this Court has granted certiorari (this Term, No. 590), illustrates the point. The **Ryan** opinion, which contains broad language as to the nature of Internal Revenue's power to investigate, was rendered on the basis of a record which plainly shows that, in the district court, an Internal Revenue Agent had testified at length in support of the administrative demand for access to books and records for closed years. In fact, the Court of Appeals for the Sixth Circuit specifically noted

2. That the ultimate thrust of the Service's argument is to reduce the role of the court to that "* * * of summarily affixing its stamp of approval to administrative action * * *" is also discussed in **O'Connor v. O'Connell**, 253 F. 2d 365, 370 (C. A. 1, 1958 and **Lash v. Nighosian**, 273 F. 2d 185, 189 (C. A. 1, 1959), *cert. den.* 362 U. S. 904 (1960).

in the **Ryan** case that the district court had been "* * * justified in concluding from the testimony of the Internal Revenue Agent that he ought not to disturb the determination made by the Secretary that the investigation was necessary" (320 F. 2d at p. 502).[3]

It is on the basis of an asserted conflict between **Ryan** and the decision of the court below in this case that the Solicitor General withdrew his opposition to the petition for certiorari in **Ryan** and acquiesced in the grant of the writ. However, as we have shown, the actual issue presented for decision in each case was entirely different. In **Ryan**, extensive testimony was presented. Here, far from adducing testimony in support of its demand, the Service has contended at all levels that it need make no showing and that its determination—that the production of records

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3. In its brief in opposition in the **Ryan** case (Br. in Opp., pp. 4-5), the Internal Revenue Service states broadly that its position has been accepted "* * * by all other courts of appeals which have had occasion to consider the question. * * *". The same contention is advanced in the petition for certiorari filed in this case (Pet., p. 11, fn. 3). On each occasion, the Service cites **Globe Construction Co. v. Humphrey**, 229 F. 2d 148 (C. A. 5, 1956); **McDermott v. John Baumgarth Company**, 286 F. 2d 864 (C. A. 7, 1961); and **DeMasters v. Arend**, 313 F. 2d 79 (C. A. 9, 1963). Each of these cases is in the **Ryan** pattern. Thus, in **McDermott**, the court of appeals specifically held that the Government had made "* * * a sufficient showing * * *" to support the district court order of enforcement. 286 F. 2d at p. 866. In **DeMasters**, the court pointed out that the burden of going forward with a justification for the investigation had been satisfied by the testimony of the Internal Revenue Agent. 313 F. 2d at p. 291. The point on appeal in **Globe** was a contention that the investigation was an unreasonable search and seizure. The opinion does not deal with the issue here presented and the record on file indicates that substantial evidence was produced by the Internal Revenue Agent involved.

The Service does not refer to **Wall v. Mitchell** 287 F. 2d 31 (C. A. 4, 1961) or **Corbin Deposit Bank v. United States**, 244 F. 2d 177 (C. A. 6, 1957), in both of which decisions the courts of appeals noted that justification for enforcement of the Internal Revenue Summons had been established by the testimony of an Internal Revenue Agent.

or testimony for closed years is necessary—is not a matter for judicial cognizance.

In its petition for certiorari in this case, the Service has particularly emphasized an asserted conflict with the decision of the Court of Appeals for the Second Circuit in **Foster v. United States**, 265 F. 2d 183 (C. A. 2, 1959), *cert. den.*, 364 U. S. 834 (1960).[4] **Foster**, again, contains broad language which seems to accept the position of the Internal Revenue Service as to the sweep of its power to obtain enforcement, and Judge Hastie, for the purpose of the opinion below, accepted the decision on this basis, noting that the decision below was "* * * contrary to the language * * *" in **Foster**. However, no square conflict between the decision of the court below and the view of the Court of Appeals for the Second Circuit can be said to exist. In **Foster**, a substantial showing was made by the Internal Revenue Agent in support of his summons. And in a subsequent decision, the Court of Appeals for the Second Circuit has seemingly retreated from the over-broad language of **Foster**. See **Application of Magnus**, 299 F. 2d 335, 337 (C. A. 2, 1962), *cert. den.*, 370 U. S. 918.

In view of what we have set forth above, it is clear, we submit, that Judge Hastie's decision is plainly correct and

4. The petition for certiorari also refers this Court's attention to pages 5-7 of the brief in opposition in the **Ryan** case and the authorities there cited. The authorities thus referred to consist, in addition to those discussed above, of the decisions of this Court in **United States v. Morton Salt Co.**, 338 U. S. 632 (1950), **Oklahoma Press Publishing Co. v. Walling**, 327 U. S. 186 (1946), and **Endicott Johnson Corp. v. Perkins**, 317 U. S. 501 (1943). These decisions, which deal with constitutional attacks upon the delegation by Congress of broad investigative powers to administrative agencies, are of no relevance here. In such cases, this Court has always adjudged the constitutional issue on the premise that the administrative investigation was within the statutory authority of the agency. Here, the scope of the Service's statutory authority is the very question at issue. Thus, in **Oklahoma v. Walling**, this Court specifically noted that the administrative official could not "* * * act arbitrarily or in excess of his statutory authority * * *" and that administrative actions were subject to judicial supervision in this respect. 327 U. S. at pp. 216-217.

careful examination discloses that the cases are not actually in conflict. The apparent difference has stemmed from efforts by the Internal Revenue Service to develop, by decision rather than by legislation, a rule of administrative convenience, namely, that no showing whatever need be made to support a demand by Internal Revenue Service for the production of books and records or the giving of testimony. The Service has done this, as in the **Ryan** case, by contending for a broad rule while, at the same time, actually [illegible]enting testimony in support of its demand. Only in the instant case has the Service actually placed its interpretation of the statute at risk by deliberately refusing, both at the administrative and at the court levels, to advance any specific reason to justify enforcement of its summons.

On the assumption that the assertion by the Solicitor General of a conflict between this case and the **Ryan** case formed at least one ingredient in this Court's determination to grant a writ in **Ryan**, respondent here has determined not to file a formal brief in opposition. However, respondent here asserts and would assert in presenting its case, that Judge Hastie's decision is entirely correct and that there is, in fact, no actual conflict of decision among the circuits. If, nevertheless, the Court is of the opinion that this case is to be reviewed, we respectfully request that the case be set down for argument with the **Ryan** case since, as the Government has urged in its petition for certiorari herein, the basic issue as to the power of the Internal Revenue Service is more squarely presented by the record in this case.

Respectfully submitted,

BERNARD G. SEGAL,
SAMUEL D. SLADE,
Attorneys for Respondents.

SCHNADER, HARRISON, SEGAL
& LEWIS,
Of Counsel.